Fiscal Note 2009 Biennium

Bill #	SB0514	**Title:**	Revise individual income tax related to interest, penalty, & federal tax refunds
Primary Sponsor:	Balyeat, Joe	**Status:**	As Amended

- ☐ Significant Local Gov Impact
- ☐ Included in the Executive Budget
- ☐ Needs to be included in HB 2
- ☑ Significant Long-Term Impacts
- ☑ Technical Concerns
- ☐ Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Expenditures:				
General Fund	$100,000	$0	$0	$0
Revenue:				
General Fund	($1,031,250)	($4,125,000)	($4,125,000)	($4,125,000)
Net Impact-General Fund Balance	($1,131,250)	($4,125,000)	($4,125,000)	($4,125,000)

Description of fiscal impact:

This bill would reduce penalty and interest on late tax payments and reduce the amount of federal income tax refunds that are subject to state income tax. These will reduce general fund revenue by $4.125 million per year after the first year implemented.

FISCAL ANALYSIS

Assumptions:

1. Section 1 of this bill requires the Department of Revenue to issue a single deficiency notice to a married couple who file separate returns on the same form regardless of whether one or both taxpayers has a deficiency assessment. It also requires the department to send a single form 1099G to married taxpayers who file separate returns on the same form (See Technical Notes 1 and 2). This will require programming changes to the department's tax processing software. These changes are estimated to have one-time costs of $100,000 in FY 2008.
2. Under current law (15-1-216, MCA), late payment penalty for non-custodial taxes is 1.2% per month or fraction of a month, with a maximum of 12%. Section 2 of this bill would make late payment penalty 0.5% per month accruing daily. This fiscal note assumes that the payments average 4.5 months late. For

payments 4.5 months late, this bill would reduce penalty from 6% (1.2% x 5) to 2.25% (0.5% x 4.5) or to 37.5% of the current amount.

3. Interest and penalty payments are tracked separately in the state accounting system for the income tax but not for most other taxes. Penalty on late income tax payments averaged $3.3 million in FY 2005 and FY 2006. Income tax is about half of the revenue the department collects, so that total penalty revenue affected by this bill is about twice income tax penalty revenue . Therefore, annual late payment penalty under current law is approximately $6.6 million. This bill would reduce late payment penalty by 62.5%, or $4,125,000.
4. Section 2 applies to penalties assessed on taxes due for reporting periods beginning after June 30, 2007. The full effect will not be seen until penalties are assessed for late payments of taxes for tax year 2008, in FY 2009. A partial effect will be seen in FY 2008 for penalties assessed on late payments of taxes that are due quarterly or monthly. The reduction in FY 2008 is assumed to be one-fourth of the full effect, or $1,031,250.
5. Under current law (15-1-216, MCA), the interest rate on unpaid individual income taxes is the higher of the IRS rate and 8%. Section 2 would remove the 8% floor. The IRS rate is set periodically at the federal short term rate plus three percentage points, rounded to the nearest whole percent. The IRS rate currently is 8%. Short term interest rates are projected to change very little through FY 2011 (HJR 2 Treasury Cash Account Interest revenue estimate) so that the IRS rate is expected to remain at 8% through FY 2011.
6. Section 3 clarifies the law relating to the inclusion of federal income tax refunds in adjusted gross income. The Department of Revenue has already adopted these provisions by rule, so this section will have no effect on revenue.
7. Under current law, taxpayers are required to pay the lower of 90% of income tax for the current year or 100% of tax liability from the preceding year through a combination of withholding and four equal estimated payments. Section 4 would prohibit the department from charging late payment interest if the taxpayer’s estimated payments are “approximately equal.” A taxpayer would owe significant late payment interest only if their earlier quarterly payments were significantly lower than their later ones. Thus, this provision is not expected to affect revenue.

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Fiscal Impact:				
FTE	0.00	0.00	0.00	0.00
Expenditures:				
Operating Expenses	$100,000	$0	$0	$0
TOTAL Expenditures	$100,000	$0	$0	$0
Funding of Expenditures:				
General Fund (01)	$100,000	$0	$0	$0
TOTAL Funding of Exp.	$100,000	$0	$0	$0
Revenues:				
General Fund (01)	($1,031,250)	($4,125,000)	($4,125,000)	($4,125,000)
TOTAL Revenues	($1,031,250)	($4,125,000)	($4,125,000)	($4,125,000)
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	($1,131,250)	($4,125,000)	($4,125,000)	($4,125,000)

Long-Range Impacts:

1. The IRS interest rate will be less than 8% in some years. In those years, the Department of Revenue will collect less in late payment interest under this bill. Penalty and interest on late income tax payments averaged $6.6 million in FY 2005 and FY 2006. About half of this is interest that would be reduced by this bill, but income tax is about half of the revenue the department collects. Therefore, annual late payment interest can be estimated to be $6.6 million. For each percentage point that the IRS rate is below 8%, annual late payment interest would be reduced by $0.825 million (1/8 x $6.6 million).

Technical Notes:

1. Section 1 of this bill requires the Department of Revenue to issue a single 1099G to married taxpayers who file separate returns on a single form. The department's legal review has determined that this conflicts with federal law and regulations governing issuance of 1099Gs.
2. Issuing a single, combined 1099G to married taxpayers who file separate returns on a single form would result in an incorrect amount of income being reported to the IRS for taxpayers who file separate federal returns.
3. Section 4 does not define "approximately equal." The Department of Revenue will have to define it through the rulemaking process.

Sponsor's Initials	*Date*	*Budget Director's Initials*	*Date*